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As I see

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ANY business, to be operated efficiently, needs a market place. While the American colonies were still young a group of men gathered daily under a butternut tree on Manhattan Island close to the present location of Wall Street to trade and exchange their securities. This eventually developed into the New York Stock Exchange. Without a common market place, shares of stock would not be liquid, and it would be impossible to determine accurately the current market value of any type of share.

There is a difference, however, between a ready market such as the New York Stock Exchange, where prices are free to fluctuate with the changes in supply and demand, and a controlled market such as the market for agricultural products, where the Government has established floors below which prices cannot drop. I am in favor of free markets, and very much opposed to controlled markets.

The Federal National Mortgage Association was established in 1938 to provide a ready market at par for mortgages insured by the FHA. In 1948 Fannie Mae was authorized to buy and sell mortgages guaranteed by the Veterans Administration. From 1938 to 1950 Fannie Mae's capital stock was owned by the Reconstruction Finance Corporation, and in 1950 it was transferred to the Housing and Home Finance Agency, which held it until 1954. Since 1954 its plan has been to mutualize the Association so that it would be owned by the mortgage interests of the United States. Unfortunately, however, mixed in with this sound idea is a return to the Welfare State philosophy that Fannie Mae can be used to support the market and to provide an outlet at par for mortgages which cannot be sold at par in the open market. This changes the concept from an open market place, with the buying and selling of real estate mortgages at prices determined by supply and demand, to a price-supporting plan in which the Federal Government in substance purchases mortgages which private investors do not consider to be worth their cost.

A scientist who had specialized in animal psychology remarked some time ago that the chief difference he had found between the reactions of lower animals and human beings seemed to be that the former learned by experience. Faced with the greatest surpluses of farm products in history we have continued to support agricultural prices above world markets, encouraging farmers to produce unusable quantities of various agricultural products. The WALL

STREET JOURNAL pointed out last month that the Government's farm program has spawned some weird by-products - eggs stored in caves, potatoes dyed blue, surplus grain piled up in circus tents, abandoned theaters and Liberty ships. At the present time it is paying farmers to build storage bins which it then rents to store surplus products for which there is no market. Many farmers have cut down, or cut out, livestock production in order to boost corn output to store at the taxpayers' expense. It quoted one farmer as saying, "When I raised hogs, I didn't have time for anything else. Hog-raising is not only hard work but it's also a year-round chore. Now I'm free in the winter. Last year, we made a two-week trip to Florida and Washington. You have a chance to make more money raising hogs but it's a lot more of a gamble."

Brazil decided to peg the price of coffee, with immediate beneficial results to its coffee growers. It did not take long, however, for Africa and other competing areas to increase their planting, with a resulting drop in exports from Brazil. The economic distress which followed threatened the continuance of the existing government, and the United States was called upon to send foreign aid to relieve the distress and political unrest. The fixing of the price of coffee affected the American consumer, not only by increasing the cost of the commodity to him, but by increasing the tax burden due to foreign aid expenditures.

The same thing, of course, is true in our domestic food situation. Wheat is made expensive to the consumer by a guaranteed price, and his purchasing power is reduced by the income taxes he pays to take care of the agricultural subsidies.

One unfortunate thing about price supports of the type that we have used in the agricultural field is that while they are reducing consumption and increasing supply, they are also accustoming the producers to an artificial market, which, after a time, becomes essential to their survival.

It seems to me that in disregarding all economic experience on the fallacy of artificially maintaining markets we are in great danger of developing the same type of situation in the real estate field which has developed in agriculture.

The home builders were originally a self-reliant group who opposed public housing because it was subsidized by the taxpayer. Now they are lobbying in Washington for a continuation of the purchasing at par by Fannie Mae of mortgages which investors are not willing to buy at that price.

By creating an artificial demand for housing, by persons unable to furnish equity money, they are encouraging many newcomers to go into the building field to satisfy this demand.

In the meantime the supply of unsold mortgages purchased by Fannie Mae continues to rise, with foreclosures on these mortgages, as would be expected, many times the national rate.

Before many years elapse the home building industry will become accustomed to this artificial volume and will need it to survive. This will mean a constantly increasing pressure for either the purchase at par of these unsalable loans or for direct Government loans to support the home building market. Some time in the future, no one can say how soon, we will find ourselves with an oversupply of housing. As vacancies increase, existing houses will sell for prices much below their cost of replacement, but because of the forced draft, construction costs will still be high. A building will not be worth what it cost to build, and the mortgages offered to the Government at par will be unsound and unsalable. At that time it will be impossible to maintain building volume regardless of the efforts made to prevent it from falling.

At the end of 1954 when the original Fannie Mae was placed in liquidation only 40% of its original FHA purchases had been sold, 11% had been repaid, 2% had been foreclosed, and 47% still remained unsold in its portfolio. In addition, 57% of all of the VA-guaranteed mortgages it had made remained unsold at that time. From December 1954 to June 30, 1958, Fannie Mae has foreclosed 7,909 FHA mortgages and 3,065 VA-guaranteed mortgages. For the entire period 51% of FHA-insured mortgages remain unsold, and 56% of VA mortgages, with a combined unpaid principal amount of $3-3/4 billion.

Because VA-guaranteed mortgages with no downpayment have been less salable on the market than the more conservative FHAs, Fannie Mae has accumulated a larger number of problem properties in this category. In 1956 only 16.5% of the foreclosures on Fannie Mae-held mortgages were VA-guaranteed. By 1957 this had climbed to 42.5%, and by 1958 to 60.2%.

I believe that at the present time Fannie Mae is being well operated within the limits prescribed by legislation. My complaint is not against its management but against the instructions it has been given by Congress. If Congress decides that mortgages are to be purchased at par by a Government agency, the agency must comply, even though it believes that this procedure is unwise. My complaint, therefore, is primarily against the type of legislation which has attempted to provide a market supported by the taxpayer for mortgages which the average mortgage lender does not believe sound.

In a bulletin I wrote more than 3 years ago* I said:

> ". . . if a mortgage lender lends more on a mortgage than a prudent lender should lend and a loss develops, at least a portion of this loss should be borne by the lender whose judgment was at

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*As I See "The Principle of the Shared Risk," April 29, 1955.

fault. Only in this way will lenders remain prudent and will losses be held to a minimum. I believe that a builder who builds a building, the cost of which is excessive from the standpoint of the current demand, should lose a portion of his capital and should not expect the Federal Government to pay the losses entailed by his lack of judgment. I believe that a promoter promoting a real estate venture should make a profit if the venture proves sound, but if the venture should be poorly conceived and poorly timed, the promoter should share in the loss. I believe that if an individual, be he a veteran or not, should decide to purchase a house, should his judgment prove false either as to location, design or type of construction, he, too, should share in the loss.

"Unless the individual citizen shares in the risk, the Federal Government will constantly have foisted upon it by various pressure groups all sorts of unwise and ill-advised methods of disposing of the taxpayers' money."

The real estate business needs a well-organized market place for the buying and selling of real estate mortgages. I am firmly convinced, however, that this market should be a free market in which the terms of sale are fixed, not by the laws of Congress but by the laws of supply and demand. There is no more reason why a mortgage should be purchased at par, regardless of all other factors, than there is for assuming that the economy would be benefited if the New York Stock Exchange, subsidized by the taxpayer, agreed that a fair market price for A T & T was $200 a share, and that all holders could turn in their stock at that price. This was tried 238 years ago in France. The French government promoted the shares of the Mississippi Company, and after a rapid rise in the price of these shares the national bank of France agreed to purchase all shares at a fixed price. This did not prevent the collapse of the Mississippi Company but it also caused a total collapse of the French currency and the French economy. In economic history this is known as the Mississippi Bubble.

The young man who believes that history started when he was born has much to learn from the past. Markets which have attempted to control prices have never worked, and while clamored for by those who believe they will benefit, generally end either in collapse or in enforced Government operation and controls.

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